

Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended.

Local Government Type <input type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Government Name Huron Behavioral Health	County Huron
Audit Date 9/30/05	Opinion Date 11/16/05	Date Accountant Report Submitted to State: 2/28/06	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- ☐ Yes ☒ No 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements.
- ☐ Yes ☒ No 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980).
- ☒ Yes ☐ No 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended).
- ☐ Yes ☒ No 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act.
- ☐ Yes ☒ No 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]).
- ☐ Yes ☒ No 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit.
- ☐ Yes ☒ No 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year).
- ☐ Yes ☒ No 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241).
- ☐ Yes ☒ No 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95).

We have enclosed the following:

	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.			✓
Reports on individual federal financial assistance programs (program audits).	✓		
Single Audit Reports (ASLGU).			✓

Certified Public Accountant (Firm Name) Nietzke & Faupel, P.C.			
Street Address 7274 Hartley Street	City Pigeon	State MI	ZIP 48755
Accountant Signature <i>Brian Hazen, CPA</i>		Date <i>2/24/06</i>	

HURON BEHAVIORAL HEALTH

HURON COUNTY, MICHIGAN

FINANCIAL REPORT
SEPTEMBER 30, 2005

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

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INDEPENDENT AUDITOR'S REPORT

To the Members of the Board
Huron Behavioral Health
Bad Axe, Michigan 48413

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Huron Behavioral Health, as of and for the years ended September 30, 2005 and 2004, which collectively comprise Huron Behavioral Health's basic financial statements as listed in the table of contents. These financial statements are the responsibility of Huron Behavioral Health's management. Our responsibility is to express opinions on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of Huron Behavioral Health, as of September 30, 2005 and 2004, and the respective changes in financial position and cash flows, where applicable, thereof, for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 16, 2005, on our consideration of Huron Behavioral Health's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in conjunction with this report in considering the results of our audit.

(Continued)

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Report of Independent Auditors (Continued)

The management's discussion and analysis and budgetary comparison information on pages iii through x and 28, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Nietzke & Faupel, PC
NIETZKE & FAUPEL, P.C.
PIGEON, MICHIGAN

November 16, 2005

HURON BEHAVIORAL HEALTH

Management's Discussion and Analysis

For the year ended September 30, 2005

This section of the Huron Behavioral Health (HBH) annual financial report presents management's discussion and analysis of financial performance for the fiscal year ended September 30, 2005 (FY05). This discussion and analysis is designed to assist the reader in focusing on significant financial issues and activities, and to identify significant changes in financial position and results of operations. Please read this section in conjunction with the auditor's report and with our financial statements, notes to financial statements and supplemental information taken as a whole.

The Michigan Department of Community Health (MDCH) contracts for Medicaid specialty supports and services through designated Prepaid Inpatient Health Plans (PIHPs) in regional geographic areas. Bay-Arenac Behavioral Health Authority (BABHA) is the designated Medicaid PIHP for a region consisting of Arenac, Bay, Huron, Montcalm, Tuscola and Shiawassee counties. HBH is affiliated with and subcontracts for Medicaid funding through BABHA, rather than directly with the state. State General Fund revenue and other state and federal grants and earned contracts are sourced directly from the state.

FINANCIAL HIGHLIGHTS

- Operating results show a deficit of \$334 thousand. Included in this result is a prior year charge of \$213 thousand for redetermination of allowable capital cost for Medicaid and State General Fund cost reconciliation purposes for FY03 and FY04. The effect of this for FY05 is a charge of \$90 thousand to the current period. Except for these issues, the operating deficit would be \$31 thousand.
- Unrestricted net assets decreased \$41 thousand or 1.2% to \$3.4 million.
- Funds restricted for capital purposes decreased \$262 thousand related to the prior year capital cost redetermination. At fiscal year end this fund balance is \$0.
- Funds restricted for risk management decreased \$18 thousand to cover State General Fund risk deficit. At fiscal year-end this fund balance is \$16 thousand.

OVERVIEW OF FINANCIAL STATEMENTS

Basic financial statements, in accordance with generally accepted accounting principles (GAAP) according to GASB 34, require the presentation of two types of financial statements. These are authority-wide statements and fund statements.

Authority-wide financial statements include the statement of net assets and the statement of activities. These provide both long-term and short-term information, and present a broad view of the overall financial status in a manner similar to a private

HURON BEHAVIORAL HEALTH
Management's Discussion and Analysis
For the year ended September 30, 2005

sector business. Information presented in these statements is on the accrual basis of accounting. Long-term assets are capitalized and depreciated. Long-term debt is recorded as a liability. Revenues are recorded when "earned" and expenses recorded when "incurred", without regard to the timing of cash receipts or disbursement.

The statement of net assets includes all assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of improving or deteriorating financial position. The statement of activities presents information showing how net assets changed during the year as a result of operating activity.

Fund financial statements contain individual groups of related accounts and are used to report current assets, current liabilities, fund balance, revenues and expenditures for specific activities or funds segregated for legal requirements or other governmental objectives. These are presented in more detail as compared to the authority-wide statements. The fund financial statements are reported on the modified accrual basis of accounting. Only those assets that are "measurable" and "currently available" are reported. Liabilities are recognized only to the extent that they are normally expected to be paid with current financial resources. Purchased capital assets are reported as expenditures in the year of acquisition. Issuance of debt is recorded as a financial resource with current year payment of principal and interest recorded as an expenditure.

Fund financial statements are divided into two categories - governmental fund financial statements and proprietary fund financial statements.

Governmental fund financial statements show how the community mental health supports and services programs were financed in the short term as well as what remains for future spending.

Proprietary fund financial statements show internal service funds reserved for risk management. These funds are held as a self-funded insurance risk reserve to protect against unanticipated current and future financial exposures related to at-risk contracts.

SUMMARY OF NET ASSETS

The following summarizes the assets, liabilities and net assets on an authority-wide basis as of September 30, 2005 and 2004.

HURON BEHAVIORAL HEALTH
Management's Discussion and Analysis
For the year ended September 30, 2005

Summary of Net Assets

As of September 30, 2005 and 2004
(In \$000s)

	<u>2005</u>	<u>2004</u>	<u>Incr/ (Decr)</u>	<u>% Change</u>
<u>Assets</u>				
Current assets	\$ 4,229	\$ 4,126	\$ 103	2.5%
Restricted assets	444	708	(264)	-37.3%
Capital assets	531	544	(13)	-2.4%
Total assets	<u>5,204</u>	<u>5,378</u>	<u>(174)</u>	-3.2%
<u>Liabilities</u>				
Current liabilities	781	637	144	22.7%
Noncurrent liabilities	428	412	16	3.8%
Total liabilities	<u>1,209</u>	<u>1,049</u>	<u>160</u>	15.3%
<u>Net Assets</u>				
Investment in capital assets	531	544	(13)	-2.4%
Restricted for capital purposes	-	262	(262)	-100.0%
Restricted for risk management	16	34	(18)	-51.9%
Unrestricted	3,448	3,489	(41)	-1.2%
Total net assets	<u>\$ 3,995</u>	<u>\$ 4,329</u>	<u>\$ (334)</u>	-7.7%
<i>Current financial position</i>	<i>3,448</i>	<i>3,489</i>	<i>(42)</i>	<i>-1.2%</i>
<i>Current ratio</i>	<i>5.4</i>	<i>6.5</i>	<i>(1.1)</i>	<i>-16.5%</i>

Current financial position is defined as the excess of current assets over current liabilities. A positive current financial position is an indicator of financial strength and an increase in current financial position is an indicator of improving financial position.

The current financial position (excess of current assets over current liabilities) is a positive \$3.4 million, a decrease of \$42 thousand or 1.2%, compared to prior year. The current ratio is the measure of current asset divided by current liabilities. The current ratio at fiscal year end is 5.4: 1, down 16.5% from 6.5:1 for the prior year.

Current assets consist of cash and investments, accounts receivable, amounts due from others and prepaid expenses. These are available for current operations and to pay current obligations. Current liabilities include accounts payable, accrued payroll, related taxes and benefits, amounts due to others and deferred revenue.

At year-end, current liabilities include \$397 thousand due to BABHA for unspent Medicaid funding from FY04 and Medicaid portion of the capital cost redetermination for FY03 and FY04, under the local service area subcontract agreement. Current liabilities

HURON BEHAVIORAL HEALTH
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also include \$20 thousand due to the State of Michigan for the State General Fund portion of the capital cost redetermination.

For the current fiscal year, there are no State General Funds left unspent and no amounts to be carried forward.

Restricted assets consist of cash, investments and accrued interest receivable. These assets are restricted for payment of compensated absences and restricted for risk management. Restricted assets of \$444 thousand have decreased by \$262 thousand or 37.3%.

At the end of FY04, assets restricted for capital purposes are \$262 thousand. This restricted fund was eliminated in FY05 a result of the redetermination of allowable capital cost. Of this amount, \$192 thousand is due to BABHA, and \$20 thousand is due to the State of Michigan, for their respective portions of the capital cost redetermination. The remaining \$50 thousand was transferred to current assets and unrestricted fund balance. This redetermination and subsequent restatement was made affiliate wide due to a BABHA decision in FY05.

Assets restricted for risk management are related to the risk obligations of the State General Fund (formula funds) risk contract. The amounts expended under the State General Fund risk contract exceeded the funding amounts provided by the state. To cover these expenditures, \$18 thousand of risk reserves and \$181k of unrestricted local funds were used. The balance in this restricted fund account has been reduced to \$16 thousand and is the equivalent of 1.6% of the funds at risk.

The remaining \$428 thousand of restricted assets are for payment of compensated absences, including certain deferred compensation amounts.

Capital assets consist of property and equipment having an estimated useful life of more than one year and original cost in excess of \$5 thousand. These assets are stated at their original book value, net of accumulated depreciation.

In fiscal 2005, \$103 thousand was expended for capital acquisitions, including \$42 thousand for land. Depreciation expense was \$110 thousand. Of this amount, \$90 thousand was related to assets acquired prior to October 1, 2003 and was not to be considered for Medicaid and State General Fund cost reconciliation purposes. The net change in capital assets was a decrease of \$13 thousand for the year. When depreciation expense exceeds capital expenditures, the net decrease represents a reduction in capital resources available for the future.

As of year-end, the net book value of depreciable capital assets was 34% of the original book value, compared to 39% at the end of the prior year. This percentage is a measure of the relative age of property and equipment. This low percentage reflects that our property and equipment is relatively old.

Noncurrent liabilities consist of the liability for compensated absences that includes vested vacation and sick pay obligations and certain deferred compensation amounts.

HURON BEHAVIORAL HEALTH
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Restricted net assets include investment in capital assets, net of related debt, and amounts restricted for risk management. These were discussed above.

Unrestricted net assets at the end of the year are \$3.4 million, a decrease of \$41 thousand or 1.2% for the year. Unrestricted net assets are 66% of total assets, up 1% from 65% at the end of the prior year.

SUMMARY OF ACTIVITIES

The following summarizes the revenue, expenses and change in net assets on an authority-wide basis for the years ended September 30, 2005 and 2004.

Summary of Activities

For the years ended September 30, 2005 and 2004
(In \$000s)

	<u>2005</u>	<u>2004</u>	<u>Incr/ (Decr)</u>	<u>% Change</u>
<u>REVENUE</u>				
Medicaid specialty supports and services	\$ 6,151	\$ 5,599	\$ 552	9.9%
State general fund priority populations	926	1,058	(132)	-12.5%
Adult benefit waiver program	114	142	(29)	-20.3%
Program service revenue	572	585	(13)	-2.1%
Grants and earned contracts	218	236	(18)	-7.7%
County appropriation	228	218	10	4.6%
Interest income	114	71	43	60.9%
Other local income	13	27	(14)	-52.8%
TOTAL REVENUE	<u>8,335</u>	<u>7,936</u>	<u>399</u>	5.0%
<u>EXPENSE</u>				
Contractual providers	1,521	1,256	264	21.0%
Program operations	5,464	5,212	252	4.8%
Managed care administration	151	119	32	26.9%
General & Board administration	1,042	968	74	7.6%
Local funds contributed to State	169	169	-	0.0%
Depreciation	110	127	(17)	-13.5%
TOTAL EXPENSE	<u>8,456</u>	<u>7,851</u>	<u>605</u>	7.7%
SURPLUS OF REVENUE OVER EXPENSE	(121)	85	(206)	
Prior year settlement	(213)	-	(213)	
CHANGE IN NET ASSETS	<u>\$ (334)</u>	<u>\$ 85</u>	<u>\$ (418)</u>	

Surplus of revenue over expenses for the current year was a deficit of \$121 thousand or 1.5% of revenue. This is a decrease of \$206 thousand from the prior year surplus of \$85 thousand. Again, \$90 thousand of this deficit is related to the non-allowability of depreciation expense for Medicaid and State General Fund cost reconciliation.

HURON BEHAVIORAL HEALTH
Management's Discussion and Analysis
For the year ended September 30, 2005

Revenue for the year was \$8.3 million compared to \$7.9 million in the prior year, an increase of \$399 thousand or 5.0% from the prior year.

Medicaid specialty supports and services revenue of \$6.2 million increased \$552 thousand or 9.9% compared to the prior year. This represents 73.8% of total revenue compared to 70.6% in the prior year. Medicaid specialty supports and service revenues are provided under a subcontract with BABHA, the Medicaid PIHP for the region. This subcontract is on a net cost not to exceed basis. There were no unspent Medicaid subcontract funds for the fiscal year.

State General Fund priority population revenue (formula funding) of \$926 thousand decreased \$132 thousand or 12.5% compared to the prior year. This represents 11.1% of total revenue compared to 13.3% in the prior year. This funding is established by MDCH as a part of the legislative appropriation process under the Michigan Mental Health Code and is used to provide supports and services to indigent priority populations, including state facility utilization and other allowable expenses. The prior year revenue included a one-time transfer of \$100 thousand transferred from an affiliate that was not available in the current year. There were no unspent State General Funds for the current fiscal year.

As previously discussed, and for the second consecutive year, the amounts expended under the State General Fund risk contract exceeded amounts provided by the state. To cover these expenditures, \$18 thousand of risk reserves and \$181k of unrestricted local funds were used. For the prior year, \$51 thousand of risk reserves and \$83k of unrestricted local funds were used. For the benefit of the priority populations, the HBH Board chose to expend local funds to cover the unfunded state obligation.

During fourth quarter, staff redefined the eligibility requirements and modified the array of services available to the people accessing General Funds. These changes were designed to manage the General Fund spending within the allocated budget amounts.

Adult Benefit Waiver revenue of \$114 thousand decreased \$29 thousand or 20.3% compared to the prior year. However, the cost of supports and services for eligible ABW beneficiaries increased \$94 thousand or 70% to \$230 thousand. HBH is fully at risk for this state benefit program. While cost in excess of revenue may be claimed as State General Fund cost, no surplus State General Funds were available. Thus, the \$116 thousand ABW deficit was required to be covered by local fund sources.

Program service revenue of \$572 thousand includes charges for services for consumers not covered by Medicaid risk subcontracts, State General Funds or other risk or grant revenue sources. These represent 6.9% of total revenue, down from 7.4% of total revenue in the prior year. These have decreased \$13 thousand or 2.1% from the prior year. This revenue is a significant source of local funds needed to meet matching fund requirements, cover funding shortfalls in other areas and contribute to unrestricted fund balance.

HURON BEHAVIORAL HEALTH
Management's Discussion and Analysis
For the year ended September 30, 2005

Grants and earned contract revenue of \$218 thousand includes revenue sources for which the use of funds is restricted to a specific purpose. These represent 2.6% of total revenue and have decreased \$18 thousand or 7.7% from the prior year.

County appropriation revenue, interest income and other local income totaling \$355 thousand are available to meet state matching fund requirements and for other local purposes. These revenue sources constitute 4.3% of revenue and have increased \$39 thousand or 12.3% from the prior year. Most of the increase is in interest income.

Total expense of \$8.5 million has increased \$605 thousand or 7.7% compared to the prior year. Most of this increase is in the provision of supports and services to Medicaid and ABW eligible beneficiaries.

Contractual provider expense of \$1.5 million includes state facility, community hospital, residential, supported employment and transportation providers. These represent 18% of total expense, and have increased \$264 thousand or 21% over the prior year.

Program operations expense of \$5.5 million includes salaries, benefits and other operating costs of supports and services programs operated directly by HBH. These represent 64.6% of total expense, and have increased \$252 thousand or 4.8% from the prior year.

Managed care administration expense of \$151 thousand includes the cost associated with these functions. These relate to at risk contracts held by HBH and functions delegated to HBH by the regional Medicaid PIHP. These represent 1.8% of total expense, and have increased \$32 thousand or 26.9% over the prior year.

General and Board administration expense of \$1.0 million represents 12.3% of total expense, and has increased \$74 thousand or 7.6% over the prior year.

Prior year settlement of \$213 thousand is related to the redetermination of allowable capital cost for Medicaid and State General Fund cost reconciliation purposes for FY03 and FY04, as previously discussed.

BUDGET

The fiscal budget process continues to be challenging due to state budget difficulties, increasing demands for entitlement services in Medicaid and other risk based programs and evolving managed care responsibilities. Unlike other local government budgets, over 86% of the HBH budget consists of risk based programs that are essentially entitled supports and services for eligible beneficiaries or priority populations. As such a majority of the expense is non-discretionary.

HURON BEHAVIORAL HEALTH
Management's Discussion and Analysis
For the year ended September 30, 2005

FUTURE OUTLOOK

The state of Michigan continues its struggle to balance budget deficits. Federal deficits are placing additional pressures on Medicaid funding. The effect of these on future funding for community mental health and specialty supports and services is unknown, but the outlook does not look favorable.

Management expects revenues to be flat at best. Support and service demand is expected to increase together with inflationary cost pressures.

Of particular concern is the State General Fund Formula Funding for priority populations under the Mental Health Code. Risk reserves and other local funds have expended for two consecutive years to cover under funded obligations. Also of concern is the funding deficit evident in the Adult Benefit Waiver Program. The ABW program is not risk adjusted for local need. Management will concentrate certain efforts to minimize State General Fund and ABW risk deficits that demand the use of local funds.

While the financial position of HBH is currently healthy, balancing the priorities and budgets will become increasingly more difficult.

* * * * *

As always, questions, comments and suggestions are welcomed from interested parties and the general public. These can be directed to management.

BASIC FINANCIAL STATEMENTS

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**STATEMENT OF NET ASSETS
SEPTEMBER 30, 2005 AND 2004**

ASSETS	Governmental Activities	
	2005	2004
CURRENT ASSETS		
Cash and investments	\$ 3,895,595	\$ 3,677,964
Accounts receivable, net	79,379	110,295
Due from other governmental units	85,273	140,489
Prepaid expenses	169,016	197,683
TOTAL CURRENT ASSETS	4,229,263	4,126,431
NONCURRENT ASSETS		
Cash - restricted	443,990	707,462
Capital assets, land	67,192	25,000
Capital assets - depreciable, net	463,787	518,928
TOTAL NONCURRENT ASSETS	974,969	1,251,390
TOTAL ASSETS	\$ 5,204,232	\$ 5,377,821
LIABILITIES		
CURRENT LIABILITIES		
Accounts payable	\$ 119,889	\$ 141,679
Due to other governmental units	468,456	315,156
Accrued payroll	180,860	164,704
Accrued payroll taxes and benefits	12,277	15,495
TOTAL CURRENT LIABILITIES	781,482	637,034
NONCURRENT LIABILITIES		
Severance pay	75,200	61,480
Accrued compensated absences	352,506	350,583
TOTAL NONCURRENT LIABILITIES	427,706	412,063
TOTAL LIABILITIES	1,209,188	1,049,097
NET ASSETS		
Investment in capital assets, net of related debt	530,979	543,928
Restricted for capital purposes		261,653
Restricted for risk management	16,284	33,746
Unrestricted	3,447,781	3,489,397
TOTAL NET ASSETS	\$ 3,995,044	\$ 4,328,724

The accompanying notes are an integral part
of the financial statements.

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**STATEMENT OF ACTIVITIES
FOR THE YEARS ENDED SEPTEMBER 30, 2005 AND 2004**

Functions	<u>Expenses</u>	<u>Program Revenue</u>		<u>Net (Expense)</u>	
		<u>Charges for Services</u>	<u>Operating Grants and Contributions</u>	<u>Revenue and Changes in Net Assets</u>	
				<u>2005</u>	<u>2004</u>
Governmental Activities					
Health & Welfare - Mental Health	<u>\$ 8,456,078</u>	<u>\$ 7,637,939</u>	<u>\$ 129,221</u>	<u>\$ (688,918)</u>	<u>\$ (231,779)</u>
General revenues					
Grants and contributions not restricted to specific programs				234,368	224,368
Unrestricted investment earnings				112,066	69,402
Restricted investment earnings				2,080	1,547
Miscellaneous revenues				6,724	21,069
Total general revenues and contributions				<u>355,238</u>	<u>316,386</u>
Change in net assets				<u>(333,680)</u>	<u>84,607</u>
Net assets - beginning of year				4,328,724	4,244,117
Net assets - end of year				<u>\$ 3,995,044</u>	<u>\$ 4,328,724</u>

The accompanying notes are an integral part
of the financial statements.

FUND FINANCIAL STATEMENTS

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**BALANCE SHEET
GOVERNMENTAL FUNDS
SEPTEMBER 30, 2005 AND 2004**

	GENERAL FUND	
	<u>2005</u>	<u>2004</u>
<u>ASSETS</u>		
Cash and investments	\$ 3,877,530	\$ 3,590,938
Accounts receivable:		
Client Services	79,379	110,295
Due from State of Michigan	28,210	85,927
Due from county	57,063	54,563
Due from internal service fund	15,661	84,623
Prepaid expenses	169,016	197,683
Cash - restricted	427,706	673,716
TOTAL ASSETS	<u>\$ 4,654,565</u>	<u>\$ 4,797,743</u>
 LIABILITIES:		
Accounts payable	\$ 119,889	\$ 141,679
Due to other governmental units	466,052	312,752
Accrued payroll	180,860	164,705
Accrued payroll taxes and benefits	12,277	15,495
TOTAL LIABILITIES	<u>779,078</u>	<u>634,631</u>
 FUND BALANCES:		
Reserved - prepaid items	169,016	197,683
Reserved - vested employee benefits	1,068,500	1,068,500
Reserved - compensated absences	352,506	350,583
Reserved - severance pay	75,200	61,480
Reserved - capital purposes	-	261,653
Unreserved	2,210,265	2,223,213
TOTAL FUND BALANCES	<u>3,875,487</u>	<u>4,163,112</u>
 TOTAL LIABILITIES AND FUND BALANCES	<u>\$ 4,654,565</u>	<u>\$ 4,797,743</u>

The accompanying notes are an integral part
of the financial statements.

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**RECONCILIATION OF THE BALANCE SHEET OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF NET ASSETS
FOR THE YEAR ENDED SEPTEMBER 30, 2005 AND 2004**

	<u>2005</u>	<u>2004</u>
Total fund balance - governmental funds	\$ 3,875,487	\$ 4,163,113
Amounts reported for governmental activities in the statement of activities are different because:		
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.		
Add: Capital assets	1,432,140	1,364,773
Deduct: Accumulated depreciation	(901,161)	(820,845)
An internal service fund is used by management to cover the risk of overspending the Managed Care Specialty Services Program contract. The assets and liabilities of the internal service fund are included in governmental activities in the statement of net assets.		
Add: Net assets of governmental activities accounted for in the internal service fund	16,284	33,746
Some liabilities are not due and payable in the current period and therefore are not reported in the funds. Those liabilities consist of:		
Deduct: Severance pay	(75,200)	(61,480)
Deduct: Compensated absences	(352,506)	(350,583)
Net assets of governmental activities	<u>\$ 3,995,044</u>	<u>\$ 4,328,724</u>

The accompanying notes are an integral part
of the financial statements.

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE - GOVERNMENTAL FUNDS
FOR THE YEARS ENDED SEPTEMBER 30, 2005 AND 2004**

REVENUES:	<u>2005</u>	<u>2004</u>
State grants		
State General Fund DCH Contract	\$ 905,099	\$ 1,057,710
Adult benefit waiver	113,562	142,491
MI Child capitation	6,720	6,602
Title XX replacement	6,118	6,118
Other state grants	<u>16,652</u>	<u>16,652</u>
Total state grants	<u>1,048,151</u>	<u>1,229,573</u>
Federal grants		
Federal block grants	36,655	56,755
PAS / ARR Grant	<u>75,914</u>	<u>78,054</u>
Total federal grants	<u>112,569</u>	<u>134,809</u>
Contributions - Local units		
County appropriation	193,250	193,250
Senior grant	<u>35,000</u>	<u>25,000</u>
Total contributions - Local units	<u>228,250</u>	<u>218,250</u>
Charges for services		
Medicaid specialty managed care capitation	5,958,952	5,599,111
Medicaid fee for service	55,443	37,139
Earned contracts	81,659	77,651
Client and third party pay	<u>516,504</u>	<u>547,325</u>
Total charges for services	<u>6,612,558</u>	<u>6,261,226</u>
Interest income	112,066	69,402
Other revenue	6,724	22,739
TOTAL REVENUES	<u>8,120,318</u>	<u>7,935,998</u>

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE - GOVERNMENTAL FUNDS
FOR THE YEARS ENDED SEPTEMBER 30, 2005 AND 2004**

EXPENDITURES:	<u>2005</u>	<u>2004</u>
Health & Welfare - Mental Health		
Personnel costs:		
Salaries & wages	3,590,691	3,441,313
Fringe benefits	1,515,902	1,412,128
Board per diem	11,200	9,568
Total personnel costs	<u>5,117,793</u>	<u>4,863,009</u>
Operating expenditures:		
Alzheimers training	19,745	17,398
Books & periodicals	1,228	2,170
Building rental	182,862	167,780
Consumer food, clothing	41,569	41,890
Contract residential	516,980	535,054
Contractual - other	295,111	512,762
Drugs & pharmaceuticals		12,683
Dues & subscriptions	8,034	7,060
Equipment rental		846
Inpatient - private	186,500	65,517
Inpatient - state	96,169	20,259
Insurance & bonds	64,351	63,212
Medical	265,688	640
Other operating expense	230,111	134,815
Printing, postage & advertising	40,692	30,122
Regional manage care administration	36,929	38,479
Repairs & maintenance	138,415	160,347

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE - GOVERNMENTAL FUNDS
FOR THE YEARS ENDED SEPTEMBER 30, 2005 AND 2004**

EXPENDITURES: (CONTINUED)	<u>2005</u>	<u>2004</u>
Operating expenditures: (continued)		
Supplies	100,534	140,708
Telephone	62,762	60,373
Travel	101,201	83,740
Utilities	62,442	51,095
Work activity	586,160	509,487
Local funds paid to PIHP	<u>168,799</u>	<u>168,799</u>
Total operating expenditures	3,206,282	2,825,236
 Capital Outlay	 103,410	 18,995
 TOTAL EXPENDITURES	 <u>8,427,485</u>	 <u>7,707,240</u>
 OTHER FINANCING SOURCES:		
Operating transfer in	19,542	55,106
 EXCESS OF REVENUES AND OTHER SOURCES OVER (UNDER) EXPENDITURES	 <u>(287,625)</u>	 <u>283,864</u>
 FUND BALANCE, OCTOBER 1	 4,163,112	 3,879,248
 FUND BALANCE - SEPTEMBER 30	 <u>\$ 3,875,487</u>	 <u>\$ 4,163,112</u>

The accompanying notes are an integral part
of the financial statements.

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED SEPTEMBER 30, 2005 AND 2004**

	<u>2005</u>	<u>2004</u>
Net change in fund balances - total governmental funds	\$ (287,625)	\$ 283,864
Amounts reported for governmental activities in the statement of activities are different because:		
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated lives as depreciation expense.		
Add: Capital outlay	103,410	18,995
Deduct: Net book value of disposals	(6,191)	(1,670)
Deduct: Depreciation expense	(110,168)	(127,356)
An internal service fund is used by management to cover the risk of overspending the Managed Care Specialty Services Program contract. The net revenue of the fund attributable to those funds is reported with governmental activities.		
Add: Interest income from governmental internal service fund	2,080	1,547
Operating transfer from internal service fund to general fund	(19,542)	(55,106)
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the funds.		
Deduct: Increase in accrual for severance pay	(13,720)	(3,480)
Deduct: Increase in accrual for compensated absences	(1,923)	(32,188)
Change in net assets of governmental activities	<u>\$ (333,680)</u>	<u>\$ 84,607</u>

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**STATEMENT OF FUND NET ASSETS
PROPRIETARY FUND
SEPTEMBER 30, 2005 AND 2004**

	<u>INTERNAL SERVICE FUND</u>	
	<u>2005</u>	<u>2004</u>
<u>ASSETS</u>		
Cash and investments	\$ 34,349	\$ 120,773
TOTAL ASSETS	<u>\$ 34,349</u>	<u>\$ 120,773</u>
 <u>LIABILITIES</u>		
Due to governmental fund	\$ 15,661	\$ 84,623
Due to affiliate	2,404	2,404
TOTAL LIABILITIES	<u>18,065</u>	<u>87,027</u>
 <u>NET ASSETS</u>		
Restricted for risk management	16,284	33,746
TOTAL NET ASSETS	<u>16,284</u>	<u>33,746</u>
 TOTAL LIABILITIES AND NET ASSETS	<u>\$ 34,349</u>	<u>\$ 120,773</u>

The accompanying notes are an integral part of the financial statements.

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**STATEMENT OF REVENUES, EXPENSES AND
CHANGES IN FUND NET ASSETS
PROPRIETARY FUND
FOR THE YEARS ENDED SEPTEMBER 30, 2005 AND 2004**

	<u>INTERNAL SERVICE FUND</u>	
	<u>2005</u>	<u>2004</u>
NON-OPERATING REVENUES:		
Interest income	\$ 2,080	\$ 1,547
INCOME BEFORE TRANSFERS	<u>2,080</u>	<u>1,547</u>
OTHER FINANCING USES:		
Transfers to governmental fund:		
Abatement of prior risk funding		(3,878)
Use of funds to finance risk	(19,542)	(51,228)
TOTAL OTHER FINANCING USES	<u>(19,542)</u>	<u>(55,106)</u>
CHANGE IN NET ASSETS	<u>(17,462)</u>	<u>(53,559)</u>
NET ASSETS - OCTOBER 1	33,746	87,305
NET ASSETS - SEPTEMBER 30	<u>\$ 16,284</u>	<u>\$ 33,746</u>

The accompanying notes are an integral part of the financial statements.

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**STATEMENT OF CASH FLOWS
PROPRIETARY FUND
FOR THE YEARS ENDED SEPTEMBER 30, 2005 AND 2004**

	INTERNAL SERVICE FUND	
	<u>2005</u>	<u>2004</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Adjustment to reconcile net income to net cash provided by operating activities:		
Decrease in:		
Due to governmental fund	\$ (68,962)	
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Transfer to governmental fund	(19,542)	
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest income	2,080	\$ 1,547
NET INCREASE (DECREASE) IN CASH	<u>(86,424)</u>	<u>1,547</u>
CASH - BEGINNING OF THE YEAR	120,773	119,226
CASH - END OF THE YEAR	<u>\$ 34,349</u>	<u>\$ 120,773</u>

The accompanying notes are an integral
part of the financial statements.

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2005 AND 2004**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

The accompanying financial statements of Huron Behavioral Health have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). In June of 1999, the GASB issued Statement 34 *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. This Statement established new financial reporting requirements for state and local governments throughout the United States. They require new information and restructure much of the information that governments have presented in the past.

Huron Behavioral Health has adopted the provisions of GASB Statement 34 for its fiscal year ended September 30, 2003. With the implementation of GASB 34, the Authority has prepared required supplementary information titled *Management's Discussion and Analysis* which precedes the basic financial statements.

Reporting Entity

Huron Behavioral Health is an Authority that operates under the provisions of Act 258 – Public Acts of 1974 (the Michigan Mental Health Code), as amended. The Authority arranges for or provides supports and services for persons with developmental disability, adults with severe or mental illness, children with serious emotional disturbance, and individuals with addictive disorder and substance abuse. These supports and services are made available to residents of the County of Huron who meet eligibility and other criteria. As the community of members, assuring local access, organizing and integrating the provision of services, coordinating care, implementing public policy, ensuring interagency collaboration, and preserving the public interest.

The accounting policies of Huron Behavioral Health conform to accounting principles generally accepted in the United States of America as applicable to governmental units.

In accordance with generally accepted accounting principles and Governmental Accounting Standards Authority (GASB) Statement No. 14 "The Financial Reporting Entity," these financial statements present all of the Authority's funds. The criteria established by the GASB for determining the reporting entity include oversight responsibility, fiscal dependency, and whether the financial statements would be misleading if data were not included.

Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e. the statement of net assets and the statement of activities) report information on all of the activities of Huron Behavioral Health. *Governmental activities* normally are supported by intergovernmental revenues.

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2005 AND 2004**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (CONTINUED)
Government-Wide and Fund Financial Statements (Continued)

The statement of activities demonstrates the degree to which the direct expenses of a function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Other items not properly included among program revenues are reported instead as general revenues. Resources that are dedicated internally are reported as general revenues rather than as program revenues.

Net assets are restricted when constraints placed on them are either externally imposed or are imposed by constitutional provisions or enabling legislation. Internally imposed designations of resources are not presented as restricted net assets. When both restricted and unrestricted resources are available for use, generally it is Huron Behavioral Health's policy to use restricted resources first, then unrestricted resources as they are needed.

Separate financial statements are provided for governmental funds and proprietary funds. Major individual governmental funds are reported as separate columns in the fund financial statements.

Measurement Focus, Basis of Accounting and Financial Statement Presentation

Government-Wide Financial Statements – The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the grantor have been met.

Fund Financial Statements – The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, Huron Behavioral Health considers revenues to be available if they are collected within 60 days of the end of the current fiscal year end. Expenditures generally are recorded when a liability is incurred, as under accrual accounting.

An exception to the "60 day" rule is the recognition of certain patient fee revenues and the related receivables. The Authority has elected to recognize these revenues on the accrual basis of accounting. The difference between the accrual basis of accounting and modified accrual basis of accounting for these revenues is not material to the financial statements.

Modifications to the accrual basis of accounting include:

- Employees' vested annual leave is recorded as expenditures when utilized. The amount of accumulated annual leave unpaid at September 30, 2005, has been reported only in the government-wide financial statements.
- Interest on general long-term obligations is recognized when paid.
- Debt service expenditures and claims and judgments are recorded only when payment is due.

(Continued)

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2005 AND 2004**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (CONTINUED)

Measurement Focus, Basis of Accounting and Financial Statement Presentation (Continued)

Proprietary Fund Financial Statements – The financial statements of the proprietary funds are reported using the economic resources measurement focus and the accrual basis of accounting, similar to the government-wide statements described above.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, are followed to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board.

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. The principal operating revenues of the internal service fund are charges to other funds for insurance services. Operating expenses for internal service funds include the cost of claims, administration and reinsurance. Any revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Fund Accounting

The financial activities of Huron Behavioral Health are recorded in individual funds, each of which is deemed to be a separate accounting entity. Huron Behavioral Health uses fund accounting to report on its financial position and results of operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. A fund is a separate accounting entity with a self-balancing set of accounts.

The financial activities of Huron Behavioral Health that are reported in the accompanying financial statements have been classified into the following major governmental and proprietary funds.

Governmental Funds

General Fund – This fund is Huron Behavioral Health's primary operating fund. It accounts for all the financial resources except those required to be accounted for in other funds.

Proprietary Funds

Internal Service Fund – This fund represents amounts restricted for risk management and set aside to fund the net uninsured exposure of potential shortfalls of DCH risk contract revenues.

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2005 AND 2004**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (CONTINUED)

Budgetary Data

Huron Behavioral Health's general fund budget is under formal budgetary control and follows both Huron Behavioral Health's and Michigan Department of Community Health's annual budget process in establishing the budgetary data presented in the financial statements. The annual fiscal budget is adopted on a basis consistent with generally accepted accounting principles and the requirements of the Michigan Department of Community Health.

Cash and Cash Equivalents

In accordance with Michigan Compiled Laws, Huron Behavioral Health is authorized to invest in obligations of the U.S. Treasury including its agencies and instrumentalities, certificates of deposit, savings accounts, deposit accounts or depository receipts of a bank which is a member of the Federal Deposit Insurance Corporation (FDIC), commercial paper rated in the three (3) highest classifications of two rating services, United States government or federal agency obligation repurchase agreements, and mutual funds composed of investment vehicles which are legal for direct investment by local units of government in Michigan.

Huron Behavioral Health's deposits are in accordance with statutory authority.

A specific amount of cash has been restricted for future payment of the compensated absences, since it has been charged to the Department of Community Health. Huron Behavioral Health has established a separate cash account to monitor this future liability.

Receivables

Uncollectible accounts are provided for using the allowance method based on historical experience and management's evaluation of outstanding accounts receivable. Based on these factors, there is an allowance for uncollectible accounts of \$31,000 and \$43,953 at September 30, 2005 and 2004, respectively.

Prepaid Expenses

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid expenses in both government-wide and fund financial statements.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2005 AND 2004**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (CONTINUED)

Capital Assets

Capital assets, which include property, plant and equipment are reported in the government-wide financial statements. Capital assets are defined by the government as individual assets with an initial cost equal to or more than \$5,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair value at the date of donation.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during construction of capital assets is not capitalized. No interest expense was incurred during the current year.

Capital assets utilized in the governmental funds are recorded as expenditures in the governmental fund financial statements. Depreciation expense is recorded in the government-wide financial statements.

Capital assets of Huron Behavioral Health are depreciated using the straight line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Land	N/A
Buildings and Improvements	20 – 30
Equipment and Furnishings	5 – 10
Computers	3
Vehicles	5

Incurred But Not Reported Claims Liability

The amounts recorded in current liabilities include amounts for incurred inpatient, residential and community provider claims liability based on management's estimate. The Authority may not be billed for these until several months after the date of service. Therefore, the liability is not liquidated within the normal 60-day period after year-end. Also, the actual cost may vary from the estimated amount for a variety of reasons that include, but are not limited to, retroactive consumer eligibility or cost recovery from other third party payers.

Deferred Revenue

Deferred revenues arise when resources are received by the Authority before it has a legal claim to them. In subsequent periods, when the revenue recognition criterion is met, or when the Authority has a legal claim to the resources, the liability for deferred revenue is removed from the fund financial statements and government-wide financial statements, and revenue is recognized.

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2005 AND 2004**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (CONTINUED)

Compensated Absences

Huron Behavioral Health's policy allows full time employees to accumulate vacation time and sick time, at various rates, depending on the employee's length of service with Huron Behavioral Health. The governmental fund financial statements record expenditures when employees are paid for these compensated absences. The government-wide financial statements record the expense and the related liability when these compensated absences are earned by employees.

Governmental Fund – Fund Balance Reserves and Designations

The governmental fund financial statements present fund balance reserves for those portions of fund balance (1) not available for appropriation for expenditure or (2) legally segregated for a specific future use. The reserves for related assets such as prepaid expenses are examples of the former. Reserves for compensated absences are examples of the later.

By resolution of the Authority's board, reserved fund balances in the amount of \$1,665,222 and \$1,939,899 as of September 30, 2005 and 2004 were established to provide for payment of future liabilities related to the following:

	<u>2005</u>	<u>2004</u>
Prepaid expenses	\$ 169,016	\$ 197,683
Compensated absences	352,506	350,583
Retirement and other post-employment benefits	1,068,500	1,068,500
Severance pay	75,200	61,480
Capital purposes	-	261,653
Total	<u>\$1,665,222</u>	<u>\$1,939,899</u>

NOTE 2 – STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY:

Budgetary Information

As set forth by State law, the CMH Board adopts an annual budget on a government wide basis. The annual budget is adopted on the full accrual basis of accounting in accordance with GASB Statement 34. The Executive Director is authorized to transfer budgeted amounts within departments; however, any revisions that alter the total expenditures must be approved by the CMH Board. For the year ended September 30, 2005, the original budgeted expenditures amounted to \$8,227,422. During the fiscal year ended September 30, 2005, the Board approved budget amendments that increased the budgeted expenditures to \$8,494,900. The government wide budget is presented in the Statement of Revenue and Expenses - Budget and Actual. All annual appropriations lapse at the end of the fiscal year.

Excess of Expenditures Over Appropriations

Budget control has been established by the CMH Board at the level of the following expenditure categories: Contractual providers, Program operations, Managed care administration, General and Board administration, Local funds contribution, and Depreciation. During the year ended September 30, 2005, Huron Behavioral Health incurred expenditures in the following categories which were in excess of the budgeted amounts:

(Continued)

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2005 AND 2004**

NOTE 2 – STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY: (CONTINUED)

Excess of Expenditures Over Appropriations (Continued)

	<u>BUDGET</u>	<u>ACTUAL</u>	<u>VARIANCE</u>
Program operations	\$5,196,898	\$5,463,694	\$(266,796)
Managed care administration	151,064	151,136	(72)

NOTE 3 - CASH AND INVESTMENTS:

As of September 30, 2005 and 2004, the Authority's cash balances are as follows:

	<u>2005</u>	<u>2004</u>
Carrying amount of cash and investments		
Unrestricted – General Fund	\$3,877,530	\$3,590,938
Restricted – General Fund	427,706	673,716
Internal Service Fund	34,349	120,773
Total carrying amount of cash and investments	<u>\$4,339,585</u>	<u>\$4,385,427</u>

The bank balances of the cash and investments are classified as follows:

	<u>2005</u>	<u>2004</u>
Insured by FDIC	\$ 876,307	\$1,076,783
Uninsured and uncollateralized	3,209,035	3,132,267
Cash management account backed by government securities	225,869	220,484
Total bank balance of cash and investments	<u>\$4,311,211</u>	<u>\$4,429,534</u>

Restricted cash balances have been set aside for the following purposes:

	<u>2005</u>	<u>2004</u>
Capital purposes		\$261,653
Payment of compensated absences	\$352,506	350,583
Payment of severance pay	75,200	61,480
Medicaid risk funding	16,284	33,746
Total restricted cash	<u>\$443,990</u>	<u>\$707,462</u>

As of September 30, 2005, the Authority had the following investments.

<u>INVESTMENT TYPE</u>	<u>FAIR VALUE</u>	<u>WEIGHTED AVERAGE MATURITY (YEARS)</u>	<u>%</u>
Government Cash Investment Fund – Comerica Bank	\$ 225,869	0.0027	100%
Portfolio weighted average maturity		<u>0.0027</u>	

1 day maturity equals 0.0027, one year equals 1.00

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2005 AND 2004**

NOTE 3 - CASH AND INVESTMENTS: (CONTINUED)

The Authority voluntarily invests certain excess funds in external pooled investment funds which included cash management funds. One of the pooled investment funds utilized by the Authority is the Government Cash Investment Fund. The Government Cash Investment Fund is an external pooled investment fund of "qualified" investments for Michigan local units of government. The Government Cash Investment Fund reports as of September 30, 2005, the fair value of the Authority's investments is the same as the value of the pool shares.

Interest rate risk. In accordance with its investment policy, the Authority will minimize interest rate risk, which is the risk that the market value of securities in the portfolio will fall due to changes in market interest rates, by; structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, thereby avoiding the need to sell securities in the open market; and, investing operating funds primarily in shorter-term securities, liquid asset funds, money market mutual funds, or similar investment pools and limiting the average maturity in accordance with the Authority's cash requirements.

Credit risk. The Authority will minimize credit risk, which is the risk of loss due to the failure of the security issuer or backer, by; limiting investments to the types of securities authorized by Board policy and state law.

Concentration of credit risk. The Authority will minimize concentration of credit risk, which is the risk of loss attributed to the magnitude of the Authority's investment in a single issuer, by diversifying the investment portfolio so that the impact of potential losses from any one type of security or issuer will be minimized.

Custodial credit risk – investments. For an investment, this is the risk that, in the event of the failure of the counterparty, the Authority will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party.

The Authority will minimize custodial credit risk, which is the risk of loss due to the failure of the security issuer or backer, by; limiting investments to the types of securities allowed by law; and pre-qualifying the financial institutions, broker/dealers, intermediaries, and advisors with which the Authority will do business.

Foreign currency risk. The Authority is not authorized to invest in investments which have this type of risk.

NOTE 4 – DUE FROM OTHER GOVERNMENTAL UNITS:

Due from other governmental units as of September 30, consists of the following:

	<u>2005</u>	<u>2004</u>
State of Michigan	\$28,210	\$ 85,927
County of Huron	57,063	54,562
Total	<u>\$85,273</u>	<u>\$140,489</u>

(Continued)

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2005 AND 2004**

NOTE 5 – CHANGES IN CAPITAL ASSETS:

The following is a summary of the changes in the depreciable capital assets of Huron Behavioral Health for the year ended September 30, 2005:

	BALANCE SEPTEMBER 30, <u>2004</u>	<u>ADDITIONS</u>	<u>REDUCTIONS</u>	BALANCE SEPTEMBER 30, <u>2005</u>
Office equipment	\$ 258,844			\$ 258,844
Computer equipment	196,333	\$ 12,661	\$23,543	185,451
Transportation equipment	629,897	30,417	12,500	647,814
Building improvement	48,124	18,140		66,264
Land Improvement	13,075			13,075
Land	25,000	42,192		67,192
Buildings	193,500			193,500
TOTAL CAPITAL ASSETS	<u>\$1,364,773</u>	<u>\$103,410</u>	<u>\$36,043</u>	<u>\$1,432,140</u>

ACCUMULATED DEPRECIATION

	BALANCE SEPTEMBER 30, <u>2004</u>	DEPRECIATION <u>EXPENSE</u>	<u>DISPOSALS</u>	BALANCE SEPTEMBER 30, <u>2005</u>	NET BOOK <u>VALUE</u>
Office equipment	\$ 141,563	\$ 21,479		\$ 163,042	\$ 95,802
Computer equipment	174,482	15,576	\$ 22,377	167,681	17,770
Transportation equipment	484,155	66,979	7,475	543,659	104,155
Building improvement	2,607	1,469		4,076	62,188
Land Improvement	327	327		654	12,421
Land					67,192
Buildings	17,711	4,338		22,049	171,451
TOTAL	<u>\$ 820,845</u>	<u>\$110,168</u>	<u>\$ 29,852</u>	<u>\$ 901,161</u>	<u>\$530,979</u>

NOTE 6 – DUE TO OTHER GOVERNMENTAL UNITS:

Due to other governmental units as of September 30, consist of the following:

	<u>2005</u>	<u>2004</u>
State of Michigan	\$ 20,448	
State of Michigan – Inpatient Care	50,697	\$ 42,151
Bay-Arenac Behavioral Health	397,311	273,005
Total	<u>\$468,456</u>	<u>\$315,156</u>

NOTE 7 – ACCRUED WAGES AND PAYROLL LIABILITIES:

This liability represents amounts paid to employees during October that were earned during September. Also included are recurring payroll liabilities that are incurred on a monthly basis.

(Continued)

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2005 AND 2004**

NOTE 8 – LONG-TERM DEBT – COMPENSATED ABSENCES:

Authority policy allows full time employees to accumulate annual leave time at various rates, depending on the employee's length of service with Huron Behavioral Health. Amounts accumulated up to a maximum of 30 days are to be paid to the employee and recognized as an expense either when annual leave time is used, or at the discretion of Huron Behavioral Health, upon termination of employment.

Employees also accumulate sick leave time at various rates, depending on the date of hire. Amounts accumulated up to a maximum of 100 days are to be paid to the employee and recognized as an expense either when sick leave time is used, or at the discretion of Huron Behavioral Health, upon termination of employment.

As of September 30, 2005, this liability was \$352,506.

The following is a summary of the changes in long-term debt of Huron Behavioral Health for the year ended September 30, 2005:

	BALANCE SEPTEMBER 30, <u>2004</u>	<u>ADDITIONS</u>	<u>REDUCTIONS</u>	BALANCE SEPTEMBER 30, <u>2005</u>
Accrued compensated absences	\$350,583	\$1,923		\$352,506
Employee severance pay	<u>61,480</u>	<u>20,835</u>	<u>\$7,115</u>	<u>75,200</u>
TOTALS	<u>\$412,063</u>	<u>\$22,758</u>	<u>\$7,115</u>	<u>\$427,706</u>

NOTE 9 – UNEMPLOYMENT COMPENSATION:

Huron Behavioral Health is a reimbursing employer for purposes of unemployment insurance claims against the employer. Huron Behavioral Health reimburses the State of Michigan for all benefits charged against it in the event of termination of employment and subsequent claims of its employees. Because an estimate cannot be made, the contingent liability for unemployment insurance claims is not recognized in the accompanying financial statements. This expense is recognized as incurred.

NOTE 10 – OPERATING LEASES:

On January 1, 2005, the Authority entered into a lease agreement with the Huron County Board of Commissioners to lease office space. The terms of the lease require monthly payments of \$11,597 for a period of one year beginning January 1, 2005. The Authority is responsible for all expenses of operation including utilities and maintenance. Future minimum lease payments at September 30, 2005 are \$34,791.

The lease further provides for cancellation by the Authority if the purpose for which the lease was entered into no longer exists due to executive, legislative or local government order or insufficient allocation of funds for this location by the Michigan State Department of Community Health and/or the Huron County Board of Commissioners.

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2005 AND 2004**

NOTE 10 – OPERATING LEASES: (CONTINUED)

The Authority entered into various lease arrangements for housing residential and day activity facilities. The terms of the leases require monthly payments amounting to \$3,641. The Authority is responsible for all expenses of operation including utilities and maintenance.

The leases also provide for an optional renewal term with monthly lease payments to be determined based on an agreed upon formula. The leases further provide for cancellation by the Authority in the event funding is terminated, reduced or licensing is withheld.

NOTE 11 – RETIREMENT SYSTEM:

The Authority participates in the Michigan Municipal Employees Retirement System, an agent multiple-employer defined benefit pension plan that covers all full-time employees. The System provides retirement, disability and death benefits to plan members and their beneficiaries. The Michigan Municipal Employees Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the system. That report may be obtained by writing to the System at 447 N. Canal Road, Lansing, MI 48917.

Under provisions of state statutes, all full-time employees must contribute 3% of the first \$4,200 of annual compensation and 5% of the portion over \$4,200 to the pension plan. In addition, the Authority must provide annual contributions sufficient to satisfy the actuarially determined contribution requirements as mandated by state statutes.

For the years ended September 30, 2005 and 2004, the Authority's annual pension cost of \$233,468 and \$234,795 for the plan was equal to the Authority's required and actual contribution. The annual required contribution was determined as part of an actuarial valuation at December 31, 2004 and 2003, using the entry actual age cost method. Significant actuarial assumptions used include (a) an 8% investment rate of return, (b) projected salary increases of 4.5% per year and (c) 2.5% per year cost of living adjustments. Both (a) and (b) include an inflation component of 3%. The actuarial value of assets was determined using techniques that smooth the effects of short-term volatility over a four-year period. The unfunded actuarial liability is being amortized as a level percentage of payroll on a closed basis.

Three year trend information:

	Fiscal year ended December 31,		
	<u>2002</u>	<u>2003</u>	<u>2004</u>
Actuarial value of assets	\$39,200,151	\$43,052,480	\$46,099,379
Actuarial Accrued Liability	46,337,177	49,259,740	52,599,796
Unfunded AAL	7,137,026	6,207,260	6,500,417
Funded ratio	85%	87%	88%
Covered payroll	11,032,137	10,901,020	11,015,228
UAAL as a percentage of covered payroll	65%	57%	59%

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2005 AND 2004**

NOTE 12- DEFERRED COMPENSATION:

Employees of Huron Behavioral Health may participate in a deferred compensation plan adopted under the provisions of Internal Revenue Code Section 457 (Deferred Compensation Plans With Respect to Service For State and Local Governments).

The deferred compensation plan is available to all employees of the Authority. Under the plan, employees may elect to defer a portion of their salaries and avoid paying taxes on the deferred portion until the withdrawal date. The deferred compensation amount is not available for withdrawal by employees until termination, retirement, death or unforeseeable emergency.

The deferred compensation plan is administered by the Michigan Association of Counties. Under the terms of an IRC Section 457 deferred compensation plan, all deferred compensation and income attributable to the investment of the deferred compensation amounts held by the Administration, until paid or made available to the employees or beneficiaries, are the property of the Authority subject only to the claims of the Authority's general creditors. In addition, the participants in the plan have rights equal to those of the general creditors of the Authority and each participant's rights are equal to his or her share of the fair market value of the plan assets. The Authority believes that it is unlikely that plan assets will be needed to satisfy claims of general creditors that might arise.

NOTE 13 – OTHER POST-EMPLOYMENT BENEFITS:

In addition to pension benefits previously described, the Authority provides post-employment benefit options for group health insurance to eligible retirees and their dependents. The benefits are provided in accordance with Authority policy. The criteria to determine eligibility include years of service and employee age. The Authority funds the benefits on a pay-as-you-go basis. Employees with at least 10 years of full time service and age 55 or older are required to pay 50% of the group health insurance premiums with the Authority paying the remaining portion of the premiums. Employees with at least 15 years of full time service and age 55 or older are required to pay 25% of the group health insurance premiums with the Authority paying the remaining portion of the premiums. Employees with at least 20 years of full time service and age 55 or older; or that have at least 10 years of full time service and age 60 or older are not required to contribute to the payment of their group health insurance premiums. During the years ended September 30, 2005 and 2004, expenditures (net of participant contributions) of \$64,187 and \$76,083 were recognized for post-employment benefits. There are 11 participants currently eligible to receive post-employment health benefits.

NOTE 14 – RISK MANAGEMENT:

General Liability:

Huron Behavioral Health participates in the Michigan Municipal Risk Management Authority, which is a public entity risk pool, for the coverage of significant losses due to its general liability. The participation in the pool constitutes transfer of the risk for significant losses to the pool with a liability limit of \$10 million. The Authority is required to pay annual premiums to the Michigan Municipal Risk Management Authority for the liability coverage. The Authority reduced their liability insurance coverage by \$5 million and settlement amounts have not exceeded insurance coverage for the current year or the three prior years. The Authority also purchased commercial insurance coverage for losses related to their property, automobiles and commercial general liability.

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**NOTES TO THE FINANCIAL STATEMENTS
SEPTEMBER 30, 2005 AND 2004**

NOTE 14 – RISK MANAGEMENT: (CONTINUED)

Workers' Compensation:

Huron Behavioral Health purchased commercial insurance to provide coverage of losses related to workers' compensation claims. The workers' compensation insurance provides coverage for up to a maximum of \$1,000,000 for each workers' compensation claim.

Employee Health Care:

For its risk of losses related to providing health care benefits to its employees and their dependents, the Authority established a partial self-insurance plan to cover claims for the medical costs of its employees and their dependents. The partial self-insurance plan provides coverage of up to \$609,924 of total medical care claims for the calendar year of 2005. For claims in excess of coverage of \$609,924, the Authority has purchased commercial insurance. Commercial insurance has also been purchased to provide vision and dental benefits for the employees of Huron Behavioral Health and their dependents. The following information relates to the Authority's partial self-insurance medical care plan for its employees:

	<u>2005</u>	<u>2004</u>
Partial self-insurance coverage limit	\$609,924	\$ 616,760
Medical care claims paid	824,571	730,535
Insurance reimbursements received	114,334	21,644
Annual medical care expense recognized	951,308	838,779

Managed Care Risk Contracts:

The Authority has a managed care risk contract with the State of Michigan for State General Fund Formula Funding for priority populations. The Authority self-insures the risk for this contract with an Internal Service Fund risk reserve. The State General Fund risk contract and reserve covers only the Authority's specific service area. The contract provides for the use of contract funds to establish the risk reserve that is restricted to meet future risk obligations. Expenditures from the Internal Service Fund risk reserve may occur if, in any one fiscal year, the Authority finds it necessary to expend more than its then current resources to provide contractually obligated supports and services for eligible individuals.

Contingent Liabilities:

Amounts received or receivable from federal, state and other grantor agencies are subject to audit and adjustment by the grantor. Any disallowed amounts, including amounts already collected, may constitute a liability. The amount, if any, of costs that may be disallowed cannot be determined at this time.

NOTE 15 – TRANSFERS BETWEEN FUNDS:

The Authority transferred \$19,542 from the Internal Service Fund risk reserve to the General Fund during the fiscal year. The transfer is in accordance with the criteria established by the Michigan Department of Community Health to meet risk corridor requirements of the managed care specialty supports and services program contracts.

REQUIRED SUPPLEMENTAL INFORMATION

**HURON BEHAVIORAL HEALTH,
HURON COUNTY, MICHIGAN**

**GOVERNMENT-WIDE
STATEMENT OF ACTIVITIES - BUDGET AND ACTUAL
FOR THE YEAR ENDED SEPTEMBER 30, 2005**

	ORIGINAL	FINAL	ACTUAL	VARIANCE FAVORABLE (UNFAVORABLE)
REVENUES:				
State grants				
State General Fund DCH contract	\$ 1,061,686	\$ 929,962	\$ 905,099	\$ (24,863)
Adult Benefit Waiver capitation	139,264	111,600	113,562	1,962
MiChild capitation	6,633	6,845	6,720	(125)
Title XX replacement	6,118	6,118	6,118	
Other state grants	16,652	16,652	16,652	
Total state grants	1,230,353	1,071,177	1,048,151	(23,026)
Federal grants				
Federal block grants	36,655	36,655	36,655	
PAS / ARR grant	80,000	80,000	75,914	(4,086)
Total federal grants	116,655	116,655	112,569	(4,086)
Contributions - local units				
County appropriation	193,250	193,250	193,250	
Senior grant	32,500	32,500	35,000	2,500
Total contributions - local units	225,750	225,750	228,250	2,500
Charges for services				
Medicaid specialty managed care capitation	6,003,625	6,092,229	5,958,952	(133,277)
Medicaid fee for service	55,878	57,858	55,443	(2,415)
Earned contracts	75,581	76,150	81,659	5,509
Client and third party payors	587,784	550,942	516,504	(34,438)
Total charges for services	6,722,868	6,777,179	6,612,558	(164,621)
Interest income	66,500	100,000	114,146	14,146
Other revenue	6,100	6,842	6,724	(119)
TOTAL REVENUES	8,368,226	8,297,603	8,122,398	(175,205)
EXPENSES:				
Health & Welfare - Mental Health				
Contractual providers	1,240,800	1,620,680	1,520,688	99,992
Program Operations	5,482,864	5,196,898	5,463,694	(266,796)
Managed Care Administration	130,900	151,064	151,136	(72)
General & Board Administration	1,075,659	1,242,081	1,041,592	200,489
Local Funds Contribution	168,799	168,799	168,799	
Depreciation	128,400	115,378	110,168	5,210
TOTAL EXPENSES	8,227,422	8,494,900	8,456,078	38,823
CHANGE IN NET ASSETS	\$ 140,804	\$ (197,297)	\$ (333,680)	\$ (136,382)

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Members of the Board
Huron Behavioral Health
Bad Axe, Michigan 48413

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Huron Behavioral Health, as of and for the year ended September 30, 2005, which collectively comprise Huron Behavioral Health's basic financial statements and have issued our report thereon dated November 16, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Huron Behavioral Health's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Huron Behavioral Health's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of management, the Board, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Nietzke & Faupel, PC
NIETZKE & FAUPEL, P.C.
PIGEON, MICHIGAN

November 16, 2005